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SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-71840; File No. SR-NYSEMKT-2014-21)

April 1, 2014

Self-Regulatory Organizations; NYSE MKT LLC; Notice of Filing of Proposed Rule Change to Make Permanent Its Pilot Program Regarding Minimum Value Sizes for Opening Transactions in Flexible Exchange Options and Establish New Minimum Value Sizes Applicable to Other FLEX Transactions and FLEX Quotes

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (the “Act”)<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that, on March 18, 2014, NYSE MKT LLC. (the “Exchange” or “NYSE MKT”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to make permanent its pilot program (“Pilot Program”) regarding minimum value [sic] scheduled to expire on March 31, 2014, and to establish new minimum value sizes applicable to other FLEX transactions and FLEX [sic]. The text of the proposed rule change is available on the Exchange’s website at [www.nyse.com](http://www.nyse.com), at the principal office of the Exchange, and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to make permanent its Pilot Program regarding minimum value sizes for FLEX Options,<sup>4</sup> currently scheduled to expire on March 31, 2014.<sup>5</sup> The Exchange believes that the Pilot Program has been successful and well-received by its membership and the investing public for the period that it has been in operation as a Pilot Program.<sup>6</sup>

Minimum Value Sizes for FLEX Options

Prior to the initiation of the Pilot Program, the minimum value size requirement for every FLEX Request for Quotes and every responsive FLEX Quote [sic] under Rule 903G(a)(4)(ii) was as follows:

- For an opening transaction (other than FLEX Quotes responsive to a FLEX Request for Quotes) in any FLEX series in which there is no open interest at the time the Request for Quotes is submitted, the minimum value size was, (i) for FLEX Equity Options, the lesser of 250 contracts or the number of contracts

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<sup>4</sup> FLEX Options provide investors with the ability to customize basic option features including size, expiration date, exercise style, and certain exercise prices. FLEX Options can be FLEX Index Options or FLEX Equity Options. The trading of FLEX Options is governed by NYSE MKT Rules 900G-909G.

<sup>5</sup> See Securities Exchange Act Release No. 69255 (March 28, 2013), 78 FR 20158 (April 3, 2013) (SR-NYSEMKT-2013-28).

<sup>6</sup> The Pilot Program was initiated on May 12, 2010. See Securities Exchange Act Release No. 62084 (May 12, 2010), 75 FR 28091 (May 19, 2010) (SR-NYSEAmex-2010-40).

overlying \$1 million in the underlying securities; and (ii) for FLEX Index Options, \$10 million Underlying Equivalent Value in the case of Broad Stock Index Group FLEX Index Options and \$5 million Underlying Equivalent Value in the case of Stock Index Industry Group FLEX Index Options. Under a prior pilot program (which was superseded by the minimum value size Pilot Program), the “250 contracts” component above had been reduced to “150 contracts.”<sup>7</sup>

Pursuant to the Pilot Program, notwithstanding the above-described rule text, the minimum size for an opening transaction in a new FLEX series is one contract. As mentioned above, the minimum value size Pilot Program is currently set to expire on March 31, 2014.

In addition to the minimum value size applicable to opening FLEX transactions in new series, as described above, Rule 903(G)(a)(iii)-(iv) prescribes minimum value sizes for other FLEX transactions and FLEX Quotes as follows:

- For a transaction in any currently-opened FLEX series, the minimum value size is (i) for FLEX Equity Options, the lesser of 100 contracts or the number of contracts overlying \$1 million in the underlying securities in the case of opening transactions, and 25 contracts in the case of closing transactions; and (ii) for FLEX Index Options, \$1 million Underlying Equivalent Value in the case of both opening and closing transactions; or (iii) for either case, the remaining underlying size or Underlying Equivalent Value on a closing transaction, whichever is less.
- The minimum value size for FLEX Quotes responsive to a Request for Quotes is 25 contracts in the case of FLEX Equity Options and \$1 million Underlying

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<sup>7</sup> See Securities Exchange Act Release No. 58037 (June 26, 2008), 73 FR 38008 (July 2, 2008) (SR-Amex-2008-50) (approval of rule change that, among other things, established a pilot program that reduced the minimum number of contracts required for a FLEX Equity Option opening transaction in a new series).

Equivalent Value in the case of FLEX Index Options or for either case the remaining underlying size or Underlying Equivalent Value on a closing transaction, whichever is less.

### Proposal

The Exchange is proposing to make the Pilot Program permanent. To accomplish this change, the Exchange is proposing to eliminate the rule text describing the Pilot Program, which is contained in Commentary .01 to Rule 903G, and to eliminate the rule text describing the pre-Pilot Program minimum value size requirements, which is contained in Rule 903G(a)(4).

In support of approving the Pilot Program on a permanent basis, and as required by the Pilot Program's approval order, the Exchange is submitting to the Commission a Pilot Program report ("Report"), which is a public report detailing the Exchange's experience with the program.<sup>8</sup> Specifically, the Exchange is providing the Commission an annual report, containing data and analysis of underlying equivalent values, open interest and trading volume, and analysis of the types of investors that initiated opening FLEX Equity and Index Options transactions (i.e., institutional, high net worth, or retail) in new FLEX series.

The Exchange believes that there is sufficient investor interest and demand in the Pilot Program to warrant its permanent approval. The Exchange believes that, for the period that the Pilot Program has been in operation, it has provided investors with additional means of managing their risk exposures and carrying out their investment objectives. Furthermore, as discussed in more detail below, the Exchange has not experienced any adverse market effects with respect to the Pilot Program.

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<sup>8</sup> A copy of the Report has been attached as Exhibit 3 to this filing.

The Exchange believes that eliminating the minimum value size requirements for opening transactions in new FLEX series on a permanent basis is important and necessary to the Exchange's efforts to create a product and market that provide its membership and investors interested in FLEX-type options with an improved but comparable alternative to the over-the-counter ("OTC") market in customized options, which can take on contract characteristics similar to FLEX Options but are not subject to the same restrictions. By making the Pilot Program permanent, market participants would continue to have greater flexibility in determining whether to execute their customized options in an exchange environment or in the OTC market. The Exchange believes that market participants would benefit from being able to trade these customized options in an exchange environment in several ways, including, but not limited to, the following: (i) enhanced efficiency in initiating and closing out positions; (ii) increased market transparency; and (iii) heightened contra-party creditworthiness due to the role of The Options Clearing Corporation ("OCC") as issuer and guarantor of FLEX Options. The Exchange also believes that the Pilot Program is wholly consistent with comments by then Secretary of the Treasury Timothy F. Geithner, to the U.S. Senate. In particular, Secretary Geithner stated that:

Market efficiency and price transparency should be improved in derivatives markets by requiring the clearing of standardized contracts through regulated [central counterparties] and by moving the standardized part of these markets onto regulated exchanges and regulated transparent electronic trade execution systems for OTC derivatives and by requiring development of a system for timely reporting of trades and prompt dissemination of prices and other trade information. Furthermore,

regulated financial institutions should be encouraged to make greater use of regulated exchange-traded derivatives. Competition between appropriately regulated OTC derivatives markets and regulated exchanges will make both sets of markets more efficient and thereby better serve end-users of derivatives.<sup>9</sup>

The Exchange believes that the elimination of the minimum value size requirements for opening transactions in new FLEX series on a permanent basis would provide FLEX-participating ATP Holders with greater flexibility in structuring the terms of FLEX Options that best comports with their and their customers' particular needs. In this regard, the Exchange notes that the minimum value size requirements for opening transactions in new FLEX series were originally put in place to limit participation in FLEX Options to sophisticated, high net worth investors rather than retail investors.<sup>10</sup> However, the Exchange believes that the restriction is no longer necessary and is overly restrictive. The Exchange has also not experienced any adverse market effects with respect to the Pilot Program eliminating the minimum value size requirements for opening transactions in new FLEX series. Again, based on the Exchange's experience to date and throughout the Pilot Program period, the minimum value size requirements are too large to accommodate the needs of ATP Holders and their customers – who may be institutional, high net worth or retail – that currently participate in the OTC market. In this regard, the Exchange notes that, prior to establishing the Pilot Program, it received numerous requests from broker-dealers representing institutional, high net worth and retail investors indicating that the minimum value size requirements prevented them from bringing transactions

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<sup>9</sup> See letter from Secretary Geithner to the Honorable Harry Reid, United States Senate (May 13, 2009), located at <http://www.financialstability.gov/docs/OTCletter.pdf>.

<sup>10</sup> See Securities Exchange Act Release No. 37336 (June 19, 1996), 61 FR 33558 (June 27, 1996) (SR-Amex-95-57).

that are already taking place in the OTC market to an exchange environment. The Exchange believes that eliminating the minimum value size requirements for opening transactions in new FLEX series on a permanent basis would further broaden the base of investors that use FLEX Options to manage their trading and investment risk, including investors that currently trade in the OTC market for customized options, where similar size restrictions do not apply. The Exchange also believes that this may open up FLEX Options to more retail investors. The Exchange does not believe that this raises any unique regulatory concerns because existing safeguards – such as certain position limit, exercise limit, and reporting requirements – continue to apply.<sup>11</sup> In addition, the Exchange notes that FLEX Options are subject to the options disclosure document (“ODD”) requirements of Rule 9b-1<sup>12</sup> under the Securities Exchange Act of 1934 (the “Act”).<sup>13</sup> No broker or dealer can accept an order from a customer to purchase or sell an option contract relating to an options class that is the subject of a definitive ODD (including FLEX Options), or approve the customer’s account for the trading of such an option, unless the broker or dealer furnishes or has furnished to the customer a copy of the definitive ODD. The ODD contains a description, special features, and special risks of FLEX Options. Lastly, similar to any other options, FLEX Options are subject to ATP Holder organization supervision and suitability requirements, such as in Rules 922 (Supervision of Accounts) and 923 (Suitability).

In proposing the Pilot Program itself and in now proposing to make it permanent, the Exchange is cognizant of the need for market participants to have substantial options transaction

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<sup>11</sup> The Exchange also notes that certain position limit, aggregation and exercise limit requirements continue to apply to FLEX Options in accordance with Rules 906G (Position Limits) and 907G (Exercise Limits). The Commission notes that certain FLEX Options do not have position or exercise limits.

<sup>12</sup> 17 CFR 240.9b-1.

<sup>13</sup> 15 U.S.C. 78a et seq.

capacity and flexibility to hedge their substantial investment portfolios, on the one hand, and the potential for adverse effects that the minimum value size restrictions were originally designed to address, on the other. However, the Exchange has not experienced any adverse market effects with respect to the Pilot Program. The Exchange is also cognizant of the OTC market, in which similar restrictions on minimum value size do not apply. In light of these considerations and Secretary Geithner's comments on moving the standardized parts of OTC contracts onto regulated exchanges, the Exchange believes that making the Pilot Program permanent is appropriate and reasonable and will provide market participants with additional flexibility in determining whether to execute their customized options in an exchange environment or in the OTC market. The Exchange believes that market participants benefit from being able to trade these customized options in an exchange environment in several ways, including, but not limited to, enhanced efficiency in initiating and closing out positions, increased market transparency, and heightened contra-party creditworthiness due to the role of OCC as issuer and guarantor of FLEX Options.

Pursuant to this filing, the Exchange proposes to adopt the existing Pilot Program,<sup>14</sup> on a permanent basis. Specifically, the Exchange proposes to eliminate all references to minimum size applicable to opening transactions in new FLEX series as presently described in Rule 903G(a)(4)(ii). The proposal to eliminate the minimum value size applicable to opening transactions in new FLEX series is similar to a rule change by the CBOE when adopting their Pilot Program on a permanent basis.<sup>15</sup>

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<sup>14</sup> See supra note 5.

<sup>15</sup> See Securities Exchange Act Release Nos. 66934 (May 7, 2012), 77 FR 27822 (May 11, 2012) (SR-CBOE-2012-040); 67624 (August 8, 2012), 77 FR 48580 (August 14, 2012) (SR-CBOE-2012-040).



Present Rules 903G(a)(4)(iii)(A)-(B) govern the minimum value size for FLEX Equity and FLEX Index Options transactions in currently opened FLEX series. Subsection (A) states that the minimum value size for FLEX Equity Options shall be the lesser of 100 contracts or the number of contracts overlying \$1 million in the underlying securities in the case of opening transactions, and 25 contracts in the case of closing transactions. Subsection (B) states for FLEX Index Options, the minimum value size shall be \$1 million Underlying Equivalent Value in the case of both opening and closing transactions. Additionally, Rule 903G(a)(4)(iv) states that the minimum value size for FLEX Quotes responsive to a Request for Quotes (“RFQ”) shall be 25 contracts in the case of FLEX Equity Options and \$1 million Underlying Equivalent Value in the case of FLEX Index Options, or for either case the remaining underlying size or Underlying Equivalent Value on a closing transaction, whichever is less. The Exchange now proposes to adopt a minimum value size of one contract when opening and closing any Equity or Index FLEX Options transaction in previously opened FLEX series and for responses to Requests for Quotes. This change, coupled with the proposed change to the minimum value size for opening transaction in new FLEX series (described above) will effectively establish a one contract minimum value size for all FLEX transactions and FLEX Quotes. A one contract minimum value size for all FLEX Options transactions and FLEX Quotes is based on similar rules governing minimum value size for FLEX Options approved for the CBOE.<sup>16</sup>

Adopting the same minimum value size for all FLEX transactions and FLEX Quotes would afford market participants, both those trading in new a FLEX series, and those trading in an existing FLEX series, equal opportunity to tailor FLEX transactions to meet their own investment objectives without being encumbered by a minimum value size. The Exchange does

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<sup>16</sup> See supra note 15.

not believe that the difference between effecting a FLEX transaction in an existing series and effecting a FLEX transaction in a new series is material to the extent that there should be different minimum value sizes for the two types of transactions. In addition, the Exchange believes it would be consistent to apply the same minimum value size to closing transactions so that investors may elect to close just a portion of their FLEX position, without being subject to a minimum value size that may be greater than the equivalent value size necessary to meet their investment objectives. Lastly, the Exchange believes that it would be consistent to apply the same minimum value size to FLEX Quotes so that market participants may respond to an RFQ with the precise number of contracts or underlying equivalent value needed to trade with a submitting OTP Holder who has requested the RFQ.

As previously stated the Exchange is submitting to the Commission a Report detailing the Exchange's experience with the Pilot Program. The Report is attached as Exhibit 3 to this filing. The Exchange notes that the Report includes data specific to the trade activity under Rule 903G(a)(4)(ii) and does not include data pursuant to subsections (iii)-(iv) dealing with opening transactions of less than 100 contracts in previously opened FLEX series, and closing transactions and responses to RFQs of less than 25 contracts, which the Exchange is proposing to amend at this time. Based on the Exchange's internal review, the Exchange believes that these types of FLEX transactions, had they been part of the Pilot Program, would be de minimis and does not believe that the absence of trade data specific to opening transactions of less than 100 contracts in previously opened FLEX series, or closing transactions and responses to RFQs of less than 25 contracts would be material to the extent that the findings in the Report would fail to provide evidence supporting the elimination of specific contract and value sizes for all FLEX transactions.

For the foregoing reasons, the Exchange believes that the proposed changes to the minimum value size for FLEX transactions and FLEX Quotes are reasonable and appropriate, promote just and equitable principles of trade, and facilitate transactions in securities while continuing to foster the public interest and investor protection.

The Exchange will continue to monitor the usage of FLEX Options and review whether changes need to be made to its Rules or the ODD to address any changes in retail FLEX Option participation or any other issues that may occur as a result of the elimination of the minimum value sizes on FLEX transactions.

In conjunction with these changes, the Exchange is proposing certain non-substantive changes to reorganize the rule text. In particular, text from Rule 903G(a)(4)(i) pertaining to the maximum 15-year term for a FLEX Option would be relocated and renumbered as Rule 903G(a)(2)(vi), [sic] As proposed, Rule 903G(a)(2)(vi) would state that the maximum term for both equity and index FLEX Options shall be 15 years [sic] In addition, the Exchange proposes to relocate relevant text pertaining to the minimum value size for FLEX Options from Commentary .02 and renumber it as Rule 903G(a)(2)(vii). As proposed, Rule 903G(a)(2)(vii) would state that the minimum value size for all FLEX Equity and FLEX Index Options transactions shall be 1 contract. The Exchange proposes renumbering present Commentary .02 as Commentary .01. These changes are proposed simply to reorganize the rule text in light of the other changes being proposed. As noted above, the changes are not substantive.

## 2. Statutory Basis

The proposed rule change is consistent with Section 6(b) of the Act, in general, and furthers the objectives of Section 6(b)(5), in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster

cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system.

Specifically, the Exchange believes that the permanent approval of the Pilot Program, which eliminates minimum value size requirements for opening transactions in new FLEX series, would provide greater opportunities for investors to manage risk through the use of FLEX Options. Further, the Exchange notes that it has not experienced any adverse effects from the operation of the Pilot Program. The Exchange also believes that making the Pilot Program permanent does not raise any unique regulatory concerns.

The Exchange also believes that eliminating the minimum value size requirements for all other FLEX transactions and FLEX Quotes, thus affording market participants on NYSE Amex Options with an equal opportunity to tailor FLEX transactions to meet their own investment objectives without being encumbered by a minimum contract size, will help to remove impediments to and perfect the mechanism of a free and open market and a national market system. In addition, offering those same market participants similar investment tools available to their counterparts on the CBOE will foster cooperation and coordination with persons engaged in facilitating transactions in securities and will help to remove impediments to a free and open market and a national market system. The Exchange believes that adopting rules similar to those approved for and utilized by the CBOE does not raise any unique regulatory concerns.

Lastly, the Exchange also believes that the proposed rule change, which provides all market participants, including public investors, with additional opportunities to trade customized options in an exchange environment and subject to exchange-based rules, is appropriate in the public interest and for the protection of investors.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Specifically, the proposal is structured to offer the same enhancement to all market participants, regardless of account type, and will not impose a competitive burden on any participant. The Exchange believes that adopting similar FLEX rules to those [sic] the CBOE will allow NYSE Amex Options to more efficiently compete for FLEX Options orders. In addition, the Exchange believes that adopting the Pilot Program on a permanent basis will enable the Exchange to compete with the OTC market, in which similar restrictions on minimum value size do not apply.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NYSEMKT-2014-21 on the subject line.

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSEMKT-2014-21. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer

to File Number SR-NYSEMKT-2014-21 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>17</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>17</sup> 17 CFR 200.30-3(a)(12).